

**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

In the Matter of
Connect America Fund
A National Broadband Plan for Our Future
Establishing Just and Reasonable Rates for
Local Exchange Carriers
High-Cost Universal Service Support
Developing a Unified Inter-carrier
Compensation Regime
Federal-State Joint Board on Universal Service
Lifeline and Link-Up

WC Docket No. 10-90
GN Docket No. 09-51
WC Docket No. 07-135

WC Docket No. 05-337
CC Docket No. 01-92

CC Docket No. 96-45
WC Docket No. 03-109

**COMMENTS OF THE CALIFORNIA PUBLIC UTILITIES COMMISSION
AND THE PEOPLE OF THE STATE OF CALIFORNIA ON THE NOTICE
OF PROPOSED RULEMAKING AND FURTHER NOTICE
OF PROPOSED RULEMAKING**

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April 18, 2011

INTRODUCTION

The California Public Utilities Commission and the People of the State of California (CPUC or California) submit these comments in response to the Federal Communications Commission’s (FCC or Commission) Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking (NPRM) seeking comments on a variety of reform steps to refocus the high cost support mechanism of the Universal Service Fund (USF) on broadband, and, in complementary steps, update the nation’s system of intercarrier compensation (ICC), control the overall size of high cost support, apply accountability criteria to supported programs, and leverage market-driven incentives.¹ The FCC’s goal is to create a “Connect America Fund” (CAF) that would “ultimately replace explicit support provided by the current high-cost fund as well as implicit subsidies from the ICC system.”² The CPUC supports these overall objectives. In summary, we support the following:

- 1) Migration of federal high-cost support to the CAF, qualified by concern about how the ‘glide path’ to this new funding would impact customers of California’s Rate of Return carriers and the equitable distribution of funding among the states, especially those states that have already made their own investments in broadband deployment;

¹ In the Matter of Connect America Fund, WC Docket 10-90; A National Broadband Plan for Our Future, GN Docket 09-51; Establishing Just and Reasonable Rates for Local Exchange Carriers, WC Docket 07-135; High-Cost Universal Service Support, WC Docket 05-337; Developing an Unified Intercarrier Compensation Regime, CC Docket 01-92; Federal-State Joint Board on Universal Service, CC Docket 96-45; Lifeline and Link-Up, WC Docket 03-109, *Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking*, rel. Feb. 9, 2011 (hereafter “NPRM”).

² *Id.*, at para. 15.

- 2) The FCC's proposed reform of intercarrier compensation as long as the 'glide path' to the FCC's ostensible objective – one low rate or bill-and-keep – is reviewed at each stage of descent in order to gauge the impact of each step on customers, carrier health, and traffic flows. The CPUC is particularly concerned about containing as much as possible the disruptive effects of the transition to IP-enabled services, applications, and interconnection while ensuring that the efficiencies, lower prices, and communications advantages promised by an IP-based communications world are achieved.
- 3) We recommend a "staircase" ascent for migration of High-Cost support to the CAF to run parallel in time with the "glide path" for reducing Intercarrier Compensation rates.

While we note that the migration to IP-enabled services, applications and networks is progressing rapidly, a ten-year migration time-frame seems a prudent interval to bring about the reforms to both Universal Service high-cost support and intercarrier compensation the FCC seeks. Our comments here join those we filed on April 1, 2011, on Section XV of the NPRM.

DISCUSSION

I. UNIVERSAL SERVICE HIGH COST SUPPORT REFORM

A. Distributions of Connect America Fund (CAF)

The FCC proposes to use a competitive bidding process, or, in the alternative, an incumbent right-of-first-refusal (ROFR) process, to identify the broadband and voice providers that would receive public high cost support and to determine the amount of

support they would receive. The ROFR price would be set by either a regression model or an engineering cost model as a competitively neutral tool to help quantify the minimum amount of public funding necessary to support broadband deployment.

California generally supports the FCC's market-based approach to determining high cost support distributions from the proposed CAF. We also generally support the concept of a forward-looking cost-revenue model to determine which unserved areas are truly uneconomic to serve without public support, and to set a benchmark price for the lowest-net-cost technology capable of providing the target level of service in those areas. However, we caution that certain aspects of the distribution mechanisms the FCC proposes could result in funding allocation distortions and inequities. First, by considering only terrestrial broadband infrastructure to determine unserved areas while disregarding available satellite service that meets the service target, funding may be skewed toward rural areas where broadband is in fact available. Second, ignoring state investments in broadband would unfairly penalize those states that already provide state funding for broadband deployment, and would discourage state broadband initiatives.

We recommend that the FCC adopt rules that would distribute federal broadband high cost support to areas of genuine need, where broadband is truly not available and where it is in fact uneconomic to provide service. The rules should also insure fairness to citizens of states that fund their own state broadband deployment programs.

California is currently a net contributor to the legacy federal universal service fund, contributing approximately 11% of the fund and receiving approximately 2.5% of

the high cost fund distributions and 8% of overall fund distributions in 2009.³ The distribution mechanism for the new Connect American Fund should not perpetuate this disparity for mixed urban-rural states such as California. To counteract any distortions in the funding methodology and to promote equity among states in fund distributions, we urge the FCC to 1) consider satellite service in determining broadband availability and in allocating support, and 2) account for state investments in broadband deployment in allocating support. In order to leverage broadband network subsidies and to maximize the benefits of these networks for all Americans, we further recommend that the FCC adopt provisions to promote the wiring of anchor institutions and broadband adoption.

The FCC should adopt a distribution mechanism that includes the parameters recommended in the discussion below.

1. Prioritization of Support Among States

The FCC asks if it should prioritize support to states that have established high-cost universal service or other broadband support mechanisms.⁴ The CPUC recommends that a minimum level of federal high cost support should be guaranteed to each state based on the state's contribution to the federal universal service fund. After the minimum level of funding is provided to each state, states that have programs to provide state subsidies for broadband deployment should get priority funding from the CAF.

Connect America Fund rules should direct funding to states, first, based on the state's contribution to the fund, or on another equity factor such as number or proportion

³ See *Universal Service Monitoring Report*, CC Docket No. 98-202 (2010), prepared by the Federal and State Staff for the Federal-State Joint Board on Universal Service in CC Docket No. 96-45.

⁴ NPRM, at para. 270.

of unserved households, in order to insure that mixed rural and nonrural states such as California do not overpay into the fund over a certain level and that rural states do not overdraw from the fund. A multi-factor approach would more fairly distribute federal funding among the states, whether they are predominantly low-density or not, and would more closely reflect the true need for broadband subsidies.

A funding mechanism that considered only whether an area is unserved and uneconomic to serve could result in a bias toward low-density areas primarily because unserved areas that are uneconomic to serve closely track areas of low population density. While the dollars needed per housing unit is lower in more densely populated counties, indicating a lesser need for public support, the number of unserved housing units in those areas is greater.⁵ We strongly agree with the FCC that broadband fund distribution should maximize the number of households and businesses passed, such as through a competitive bidding process which ranks bids by dollars per households passed from lowest to highest.⁶ A funding mechanism that accounts for an equity factor such as number or proportion of unserved households would offset a bias toward rural geographic areas with few housing units per square mile.

As a corollary, in first allocating funding at the state level, the FCC could use a statewide analysis to identify transportation corridors that could be targeted for middle mile deployment. Transportation corridors would be technology and industry neutral, just as counties are, and since census block groups do not cross county lines, county data

⁵ See Map of Unserved Housing Units per Square Mile, FCC Omnibus Broadband Initiative Technical Paper No. 1 (April 2010), at p.9, Appendix B.

⁶ NPRM, at para. 419.

would be compatible with other data collected by census block groups, such as the mapping data the CPUC is collecting under its Recovery Act mapping grant.⁷ Targeting funds to statewide or cross-border projects using highway rights-of-way would leverage existing public and private assets. Furthermore, a statewide analysis would provide an alternative basis for funding that is not primarily associated with population density.

After minimum base funding is guaranteed to each state, based on an equity factor, additional priority funds should be allocated to states that provide state subsidies for broadband deployment. The FCC should devise funding rules that give states an incentive to invest in their own network infrastructure rather than merely relying on federal support. If funding were based only on a funding shortfall, states with their own state broadband deployment programs would not only lose initially but also would be disadvantaged throughout the life of the fund. Citizens in states with their own programs could pay twice—they would overpay into the federal fund, while also paying for the state program.

We have previously recommended that states providing matching funds for the federal subsidies be awarded supplemental funding, while states that do not provide matching funds receive only base level funding,⁸ and we reiterate that recommendation. Such a mechanism would reward states that have already used their own resources to extend broadband availability and would encourage other states to do so. States that have

⁷ American Recovery and Reinvestment Act of 2009, P.L. 111-5 (Recovery Act).

⁸ Comments of the California Public Utilities Commission, *In the Matter of Comments Sought on the Role of Universal Service Fund and Intercarrier Compensation in the National Broadband Plan Comments NBP Public Notice #19*, GN Docket No. 09-47, GN Docket No. 09-51, GN Docket No. 09-137, December 7, 2009, at p. 5.

successfully implemented a state matching fund program for Recovery Act grants are already well-positioned to make such commitments.

California has its own state broadband grant program, the California Advanced Services Fund (CASF). In 2009, California citizens contributed a 0.25% surcharge on each of their telephone bills to our state Advanced Services Fund; these contributions were in addition to the surcharges California citizens contributed to the federal high cost fund. If federal funding for broadband were based only on level of public support needed to build networks in unserved, uneconomic areas, California citizens would be doubly burdened, having contributed more but then receiving correspondingly less because of those very contributions.

2. Satellite Service Should Be Supported Where Appropriate

The FCC asks about the role of satellite and, in particular, whether it should allow satellite broadband providers to partner with terrestrial broadband providers that bid for support.⁹ The FCC also asks if it should estimate costs of providing service using the lowest-cost (or lowest-net-cost, if revenues are taken into account) technology capable of providing the required minimum level of voice and broadband service for each area.¹⁰

We recommend that the FCC take satellite service into consideration when identifying unserved areas, and that it include satellite as a technology option for support. CAF rules should permit universal service funding for satellite where it meets universal service goals and relevant performance metrics.

⁹ NPRM, at para. 424.

¹⁰ *Id.*, at para. 272.

Considering satellite service availability in the identification of unserved areas would “true up” the distribution mechanism by removing from the process the areas that do in fact have broadband available by satellite. Many sparsely populated areas already have broadband availability at a speed that can provide streaming video; including satellite in the model would help target CAF funding to areas of true need. According to an industry analysis, satellite customer areas are a proxy for areas unserved by wireline broadband and 75% of satellite customers are in areas with fewer than 100 homes per square mile.¹¹ The FCC should include satellite broadband in its analysis, because satellite service is already or soon-to-be available in many remote areas that would otherwise be identified as lacking in broadband availability.

Satellite service at the target speed is already available in many remote areas that the FCC would identify as lacking in broadband availability, and the satellite industry has announced plans to launch new satellites with higher bandwidth and service quality capabilities that would go even farther to fill the availability gap identified by the National Broadband Plan.¹² Since the Plan was published last year, LightSquared launched SkyTerra-1 in November 2010, the third U.S. satellite operator to launch a mobile broadband satellite for U.S. consumers (after DBSD North America’s ICO-G1 satellite and TerreStar Networks’ TerreStar 1 spacecraft.);¹³ ViaSat Inc. has scheduled the

¹¹ *Ex Parte* Communication of ViaSat, Inc., GN Docket 09-51; WC Docket No. 10-90; WC Docket No. 05-337, June 7, 2010.

¹² *Satellite Broadband Industry Looks To Overcome Image Problem*, 03/18/10 Spacenews.com. http://www.spacenews.com/satellite_telecom/100318-satellite-broadband-has-reputation-problem.html . See also *ViaSat on New Trajectory Following Deal to Create Satellite-Based High-Speed Internet*, Xconomy.com, February 3, 2010.

¹³ <http://www.spacenews.com/launch/101115-proton-lofts-skyterra.html>

launch of its high-capacity satellite ViaSat-1 for summer 2011,¹⁴ and Hughes plans to launch its high-capacity Ka-band satellite Jupiter in 2012.¹⁵

While the FCC has noted that “the latency associated with satellite would affect the perceived performance of applications requiring real-time user input,”¹⁶ satellite is competitive with wireless terrestrial broadband in many areas, since wireless quality varies with location and time, depending on propagation characteristics and traffic volume. ViaSat, Inc., one of the two companies that have announced plans to launch a new satellite in 2011, claims that improvements in satellite technology will make it competitive with terrestrial alternatives, particularly in speeds but also in quality of service relative to cost.¹⁷

The FCC staff itself includes satellite as a technological alternative in the FCC’s Rural Broadband Report. The Rural Broadband Report declares that solutions should reflect the full range of technological options, including satellite.¹⁸

Finally, there is a strong case from a cost-benefit standpoint to consider satellite service. The FCC’s National Broadband Plan stated that broadband-over-satellite is a cost effective solution for low-density areas and could reduce the \$24 billion total

¹⁴ <http://www.viasat.com/news/viasat-reschedules-launch-viasat-1>

¹⁵ <http://spacefellowship.com/news/art19940/arianespace-signs-contract-with-hughes-to-launch-jupiter.html>

¹⁶ *In the Matter of Connect America Fund, a National Broadband Plan for Our Future; High Cost Universal Service Support*, WC Docket No. 10-90, GN Docket No. 09-51, WC Docket No. 05-337, Notice of Inquiry/Notice of Proposed Rulemaking, FCC 10-58, Appendix C, p. 89 (rel. Apr. 21, 2010) (“CAF NOI/NPRM”).

¹⁷ *Id.*

¹⁸ FCC, *Bringing Broadband to Rural America: Report on a Rural Broadband Strategy*, at p. 4 (May 22, 2009).

investment gap by \$14 billion, if used to reach the 250,000 most-expensive-to-reach housing units.¹⁹ Funding for infrastructure build-out should be analyzed in concert with funding for user support and adoption initiatives; considering satellite in determining broadband funding would free scarce federal dollars for broadband adoption initiatives such as user subsidies and other targeted programs.

3. Stand-alone Voice Service Support Should Be Continued

California recommends that the FCC require CAF recipients to offer voice as a stand-alone service, with such voice service held to the same quality of service standards are provided today by the PSTN, including access to E911, voice quality, and such vertical features as caller-ID.

California state telecommunications policy is to assure the affordability, as well as the availability, of high-quality telecommunications services to all Californians. The CAF should support voice as a standalone service, with all the service quality features of traditional telephone service, so as to insure the availability of affordable voice service for all Americans even as network infrastructure migrates to IP-enabled facilities.

4. ETC Designation and Service Areas

States should retain the ability to designate eligible telecommunications carriers (ETCs) and set their own public interest standards for such designations.

The FCC asks about the role of states, territories, and Tribal governments in monitoring the public interest obligations of CAF recipients, and whether they should be

¹⁹ CAF NOI/NPRM, at Appendix C, p. 89.

permitted to establish additional public interest obligations for CAF recipients.²⁰ In order to better insure the integrity of the new program, the FCC should provide for a strong state role in the oversight of federally-supported broadband projects within their own states, including state designation of ETCs and setting and enforcement of ETC obligations. The FCC should delegate to the states the oversight authority over the pricing, quality, and service continuation requirements of the subsidies awarded within the state, as well as authority over company eligibility for support.

Federal broadband subsidies should come with conditions attached, to insure affordability, quality of service, and continuation of service to users during the transition to broadband and beyond. Imposing pricing constraints on subsidy recipients would keep subscription costs low and help close the adoption gap as well as the availability gap. State oversight would promote effective enforcement of those requirements, since states have an overriding interest in insuring broadband availability to their own citizens. State commissions are the optimal enforcement entities for ETC requirements and federal funding requirements, because they have a thorough and intimate understanding of the particular conditions in their own states and, through their ongoing public proceedings and processes, are more closely connected to the communications needs of their citizens.

5. Avoiding a New Digital Divide

The FCC should establish comparable broadband performance milestones across urban and rural areas so that consumers in rural areas are not subjected to a lower speed standard for Internet connections.

²⁰ NPRM, at para. 315.

While we would support programs to provide high speed broadband connections to anchor institutions in densely populated areas, comparable broadband milestones matching urban areas should be maintained for rural areas, so that consumers in rural areas are not subjected to a lower speed standard for Internet access. The USF has not supported inferior phone service for rural and high cost areas as a penalty for public support, nor should it do so for Internet access.

6. Infrastructure Sharing

Universal service funding rules should encourage sharing of infrastructure, by prioritizing the wiring of anchor institutions in unserved and underserved areas.

The FCC asks about policies to encourage sharing of infrastructure.²¹ Sharing supported infrastructure becomes crucial in the context of anchor institutions.²²

Universal service funding can best achieve support synergies and operational efficiencies when the broadband connectivity for schools, libraries, and rural health care facilities are widely shared. Where build-out is required to connect anchor institutions — for example, through the construction of lateral connections to regional fiber networks — recipients of CAF funding should have obligations to connect anchor institutions in the communities in which they serve residential customers.²³

California's own state broadband programs support not only Internet and voice services for anchor institutions, but also construction projects that connect anchor institutions to middle mile transport, or that build middle mile transport to connect anchor

²¹ NPRM, at para. 148.

²² NPRM, at para. 148.

²³ *Id.*, at para. 149.

institutions to Internet collocation hubs. The California Teleconnect Fund²⁴ provides a 50% discount on broadband and voice services to qualifying schools, libraries, government-owned and operated hospitals and health clinics, and community based organizations.²⁵ The California Advanced Services Fund (CASF)²⁶ provides grants for middle mile connections to anchor institutions.

For example, in October 2010, the CPUC approved a CASF matching grant of \$6,659,967 to the Central Valley Independent Network (CVIN) project. CVIN will build, operate and maintain a middle mile fiber-optics network serving 18 Central Valley counties: Amador, Calaveras, Colusa, El Dorado, Fresno, Kings, Kern, Mariposa, Merced, Madera, Nevada, Placer, San Joaquin, Stanislaus, Tuolumne, Tulare, Sutter, and Yuba. CVIN will also build a last mile WiMax wireless network in Fresno, Tulare, Kings, and Kern Counties to bring high-speed broadband access for the first time to unserved, rural communities containing 710,102 residents, 206,764 households, and 20,502 businesses. In addition, 60 anchor institutions will be connected to each other at network speeds of between 1-10 Gigabits: 11 community college districts, 19 county Offices of Education sites, three CSU universities, 20 county libraries, and seven public safety sites. Through this project, health facilities in 18 counties will also be connected to the California Telehealth Network. The CASF grant represented 10 percent of the broadband infrastructure project costs of \$66.60 million and directly leverages a \$46.62

²⁴ See CPUC Decision 96-10-066 (Oct. 25, 1996).

²⁵ <http://www.cpuc.ca.gov/PUC/Telco/Public+Programs/CTF/>

²⁶ See CPUC D.07-12-054 (Dec. 20, 2007).

million dollar grant from federal funding provided through the American Reinvestment and Recovery Act.

7. Funding Priorities Among Federal USF Programs

As a general matter, we urge the FCC to consider universal broadband service policies comprehensively. The FCC asks whether, in determining the size and role of the CAF, it should take into account the cumulative effect of the four support programs, acting together, to achieve the goals of universal service.²⁷ In determining the size and role of the new high cost support program, the FCC should take into account the cumulative needs of the four current federal universal service programs (high-cost, low income, schools and libraries, and rural health care), acting together, to allow for possible reprioritization of CAF monies to the other programs.

The FCC should consider broadband availability and broadband adoption efforts in concert. It should use broadband funding, whether provided to companies for network build-out or to users for Internet connections, to promote the adoption as well as the availability of Internet access everywhere in the country. Again, funding for infrastructure build-out should be analyzed in concert with funding for user support and adoption initiatives so as to free scarce federal dollars wherever possible for much-needed broadband adoption initiatives such as user subsidies and other targeted programs. While some may believe that closing a 5% broadband “availability gap”²⁸ is our most

²⁷ NPRM, at para. 416.

²⁸ FCC, National Broadband Plan, Chapter 8.

pressing need, we believe that a 35% broadband adoption digital divide is an equally urgent national priority.

In this regard, the FCC should reallocate funding from broadband deployment to broadband adoption programs as the network is built out in order to get the greatest benefit in terms of households connected for the dollars spent.

A need for new broadband networks will continue to emerge as new housing units are built. As federal broadband infrastructure subsidies bring the nation to near-100% availability, then federal subsidies need continue only to the extent necessary to meet the ongoing network needs. As the nation reaches the target speed for all, it is unclear whether there will be a rationale for company subsidies, other than to maintain universal availability by building in greenfield areas. If there is no such need, we may potentially move away from network subsidies to end user supports only. If there is a greater demand for Lifeline and anchor institution discounts, those should be favored over direct provider support where possible. The pursuit of adoption should succeed availability as a target for support.

As the nation moves toward universal broadband service, federal broadband subsidies can shift from the supply side (subsidies to companies that own and operate broadband-capable networks) to the demand side (subsidies to residential Internet users) as needed. Moving subsidies from the supply side to the demand side as program goals are met would obviate problems that have been endemic to the telephone universal service funding program, where states with varying population densities subsidize states with sparse population densities. The Connect America Fund provides an opportunity to

learn from our experience and structure the new program differently to avoid similar problems.

II. INTERCARRIER COMPENSATION

The FCC takes its lead from the Joint Board's recommended principle "that universal service support should be directed where possible to networks that provide advanced services, as well as voice services."²⁹ The FCC states that "[w]e believe this principle strikes a reasonable balance between the goal of preserving and advancing universal service as currently supported and the goal of increasing access to advanced telecommunications and information services."³⁰ We concur.

The current federal high cost mechanism is designed to subsidize the costs of networks that provide voice services in high cost areas, so the federal high-cost mechanisms do not currently target support toward extending or maintaining broadband service to unserved high cost areas. California agrees with the FCC's long range goal for high-cost support reform: that legacy high-cost programs be replaced by a new support mechanism, the Connect America Fund, that extends the universal voice-centric connectivity Americans have come to expect and rely upon to a universal advanced broadband access, as well as to the applications that such access will bring for the 21st century.

In order to achieve this transition to the CAF, the FCC recognizes that intercarrier compensation reform is necessary to eliminate waste and inefficiencies in the ICC

²⁹ NPRM, at para. 58, citing Joint Board 2010 Recommended Decision, 25 FCC Rcd at 15625, para. 75 (NPRM fn. 67).

³⁰ *Id.*

system, and to “create the proper incentives for carriers to invest in new broadband technologies so that consumers have the opportunity to take full advantage of the new capabilities of this broadband world.”³¹

As the FCC also points out, the current intercarrier compensation regime “is not sustainable in an all-broadband Internet Protocol (IP) world where payments for the exchange of IP traffic are not based on per-minute charges, but instead are typically based on charges for the amount of bandwidth consumed per month.”³² The FCC lists the advantages of unshackling intercarrier compensation from this legacy system as including costs savings from eliminating circuit-switching and switching costs, savings from reductions in space needs, lower utility costs, and “the elimination of other signaling overhead.”³³

A. Necessary Steps to Achieve Intercarrier Compensation Reform

In two separate places in the NPRM, the FCC lists possible “end-point” intercarrier compensation methodologies for an all-IP network, including compensation methodologies for VoIP traffic.³⁴ The various approaches include adoption of bill-and-keep, the adoption of flat-rated intercarrier charges, or the immediate obligation to pay existing intercarrier compensation rates (for VoIP traffic). These are presented as

³¹ NPRM, at para. 505.

³² *Id.*, at para. 505, quoting the National Broadband Plan at 142.

³³ *Id.*, at para. 506. At para. 527, the FCC states: “Most fundamentally, the long-term approach to intercarrier compensation reform also must be consistent with the exchange of traffic on an IP-to-IP basis Voice traffic exchanged on an IP-to-IP basis can simply involve the exchange of packets, and does not require occupying an entire circuit for the duration of the call as in a circuit-switched network.”

³⁴ *Id.*, at paras. 530-532, and again at paras. 615-619 (discussing glide path for VoIP traffic).

discrete methodologies or approaches. But given the context of a transition to a new intercarrier compensation system or regime, they become more useful as integrated steps to be taken over the duration of the transition, but in the reverse order in which they are presented in the NPRM. Thus, the transitional steps of the proposed “glide path”³⁵ would be as follows:

1. The first step would be the immediate adoption of existing intercarrier compensation rates, with a reasonable interval of time for states to bring intrastate rates into alignment with interstate rates;
2. The second step would be adoption of a defined uniform rate lower than existing intercarrier compensation rates, for both interstate and intrastate intercarrier compensation and reciprocal compensation;
3. The third step would be the adoption of a still lower uniform rate such as the one suggested in the NPRM, \$0.0007, as a last step before the FCC’s apparent objective, bill-and-keep.
4. The final step – if indeed the previous steps are judged to be successful in achieving the FCC’s stated objectives for universal broadband service – would be bill-and-keep except where traffic imbalances justify tailored interconnection agreements to cover such traffic, which states will supervise using the criteria of what constitutes just and reasonable pricing.

This approach is consistent with the one outlined in Section XIII of the NPRM, in particular paragraph 534. There, the FCC anticipates the following steps in what it

³⁵ *Id.*, at para. 617.

describes as a first option for modernizing intercarrier compensation rules to encourage migration to advanced IP-networks, where the transition would be implemented through reliance on the existing roles played by the states and the Commission with respect to regulation of rates:

- Partnership with the states to reform ICC;
- FCC reduction of *interstate* access charges in announced steps;
- FCC adoption of a methodology for states to use to reduce reciprocal compensation rates;
- States remain responsible for reforming *intrastate* access charges, including intrastate access charges paid by wireless carriers to LECs.
- States that align intrastate rates with the FCC interstate rates in an expedited fashion would have first call on CAF funding.³⁶

These steps should meet the test of the objective described in paragraph 534, to unify all intercarrier rates, including those for intrastate calls. Reduction and unification of rates would have the advantages sought by the FCC: reduction in arbitrage opportunities, minimizing disruption to customers and service providers, and providing the FCC with the ability to modulate the impact on the CAF. However, the reduction of access rates also raises complex issues with potentially significant adverse impact on end use customers that states are in a better position to explore and address. Therefore, the FCC should retain existing jurisdictional roles with states responsible for intrastate access

³⁶ *Id.*, at para. 544. Alignment of intrastate ICC rates with interstate rates would be the test of whether the state in question would receive a preference for receipt of early CAF funding.

charge reform. Federal and state roles can best be harmonized through policy guidance from the FCC, with states retaining the flexibility to implement national policy in accordance with the FCC's guidelines. The overall objective is to develop a full IP-based telecommunications system, where access charges are uniform regardless of who initiated the traffic or terminated it, or whether the traffic is intrastate or interstate. States are capable of engaging in access charge reform in a manner consistent with federal law and policy.

B. Developing a Recovery Mechanism

We agree with the FCC's recognition that "today we are faced with a telecommunications industry transitioning to all-IP networks."³⁷ The point of the universal service reform recommended by the FCC and endorsed above, is to "reinforce, and facilitate, this trend" to make universally available IP-enabled services and applications.³⁸ As the FCC further notes, "non-regulated services are an increasingly important source of revenues derived from multi-purpose networks."³⁹ The FCC draws a conclusion we share: "... our analysis of recovery needs should not be limited to the voice-centric approach that has tended to characterize prior reform efforts."⁴⁰

In structuring a recovery mechanism and evaluating the need for recovery, the FCC should do as its "no barriers" approach suggests: evaluate total company regulated and non-regulated revenues. A revenue recovery test should recognize, as the FCC notes,

³⁷ *Id.*, at para. 561.

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

that “a significant portion of rate-of-return carriers’ costs, including costs of upgrading the network with fiber for broadband, is allocated to regulated services, even though non-regulated services increasingly have been provided using that same network, and have accounted for an increasing percentage of revenue.”⁴¹ We share the FCC’s sentiment that “[a]s a policy matter, when evaluating recovery in the context of intercarrier compensation reform, it is unclear why the Commission would simply ignore all revenues from such [non-regulated] services.”⁴² We note that the authors of the Omaha Plan propose “that the USF contribution mechanism should be expanded to include total revenues for all telecommunications and information service providers....”⁴³ They use FCC Form 499 data to estimate that with \$448 billion in total revenues annually, the USF contribution factor could be reduced to 1.8% from the current contribution factor of 15.5% (as of their writing).⁴⁴ Similarly, it is appropriate for the Commission to take into consideration costs savings to carriers and service providers associated with less costly IP-enabled capabilities – which should moderate revenue recovery draws on the CAF and rate impacts on customers.⁴⁵

The FCC also seeks comment on proposals to recover first from end users, such as through a rate benchmark as a means of accounting for existing revenue streams, and the

⁴¹ *Id.*, at para. 569.

⁴² *Id.*

⁴³ *The Omaha Plan, A White Paper to the State Members of the Federal-State Joint Board*, Robert Haga, Kathy Hagans, Jing Liu, and Earl Poucher, Feb. 7, 2011, p. 4.

⁴⁴ *Id.*

⁴⁵ NPRM, at para. 572.

appropriate role, if any, of interstate subscriber line charges (SLCs).⁴⁶ We have no comment at this time on the advisability of the FCC establishing a residential rate benchmark or reconfiguring SLCs. We reserve the right to comment on this at a later date, if appropriate.

C. Special Recovery Considerations for Rate-of-Return Carriers

In Appendix D of the FNPRM,⁴⁷ the Commission attempts to establish a mathematical framework that might be used to calculate payments from the Connect America Fund to rate-of-return (ROR) carriers to offset the elimination of both interstate and intrastate switched access charges. Unfortunately, this framework is only conceptual in nature and has too many unknown variables to enable us to calculate what the dollar impact would actually be. Given this uncertainty regarding specifics and traceable variables, it is not possible at this time to support this framework as a tool for calculating the adequacy of replacement payments.

However, the adoption of a ten-year transition period for the Commission's glide path for unifying ICC rates would allow verification of funding impacts without dependence on a mathematical formula with uncertain inputs. If a ten-year transition is deemed a reasonable time-frame to move access charges from their current levels to zero, which would be the case under a bill-and-keep regime, there should be a similar time frame to transition the ROR carriers from their current high-cost funding support to the

⁴⁶ *Id.*, at paras. 559, 573-584.

⁴⁷ *Id.* Appendix D, "Incentive Regulation: A Framework for Calculating Inter-carrier Compensation Replacement Payments for Rate-of-Return Carriers," pp. 245-247.

CAF, since a much larger percentage of their high-cost support comes explicitly from existing high-cost funding than implicitly through access charges.⁴⁸

The CPUC understands that the Commission does not intend to eliminate all high-cost support at the outset of its reform process, but rather intends to transition away from the current high-cost support structure to the CAF over a transition period. In fact, both type of funds, high-cost and CAF, will coexist for some period of time, with those carriers currently receiving high-cost support continuing to do so, albeit perhaps at a lower level than they are currently, and others receiving CAF money to build out broadband to unserved areas. As the Commission proposes at paragraph 280 of the NPRM:

Given our objective of extending broadband to unserved housing units in as efficient a manner as possible, we propose that *only one entity in any given geographic area receive support in the first phase of the CAF*. We seek comment on this proposal. In some instances, *the current incumbent ETC may also be the winning bidder for CAF support*. In others, *another entity could win CAF support for deploying broadband in the unserved area, but the current incumbent would continue to receive support for its entire study area under existing support mechanisms as modified*. [Emphasis added.]

How this process is modulated in practice will become critical. If an entity other than the incumbent ETC becomes the recipient of support, the “as modified” qualification regarding support for the incumbent ETC in the above paragraph will need more precise definition, and the duration of that support will need to be clarified.

⁴⁸ For rate of return carriers in California, access charges revenue accounts for a little over 15% of the combined sum of access charge and high-cost fund revenue.

We understand that long term goal of the FCC is to eventually eliminate the current high-cost support fund in its entirety. It is unclear how that objective is squared with the above intention to continue existing support mechanisms to existing recipients who may not become the “one entity” receiving support in the first phase of the CAF. This raises obvious questions about the overall demand on support funds and the duration of any overlapping support expenditures, as well as the size of the CAF. We are therefore of the view that the transition must be measured, with a glide path sufficient in terms of time and incentives to allow the ROR carriers to have an opportunity to adapt to these new funding mechanisms and to the withdrawal of the old. Alternatively, as suggested by the Commission, the ROR carriers could be treated differently within the new CAF structure, with funding levels reset periodically to allow for an appropriate rate of return.⁴⁹ We reserve comment on any such special treatment until more detailed recommendations are forthcoming from the FCC or from other parties to this proceeding.⁵⁰

The FCC states that “given the Commission’s long-term vision for the CAF, we anticipate that intercarrier compensation replacement funding would *not* exist as a distinct CAF component. Rather ... such funding could be subsumed within the support provided to serve a particular geographic area under either a right of first refusal or

⁴⁹ NPRM, at para. 452.

⁵⁰ In the NPRM, the FCC states: “We seek comment on whether the Commission should initiate a proceeding to represcribe the authorized rate of return for rate-of-return carriers if it determines that such carriers should continue to receive high-cost support under a modified rate-of-return system.” NPRM, at para. 456.

competitive bidding approach.”⁵¹ Thus, the critical questions the FCC needs to clarify are how the CAF would support broadband deployment in practice after intercarrier compensation mechanisms are replaced by much reduced uniform access rates or bill-and-keep, and how recipients of federal support are identified, their support determined, and their performance audited when support may be detached from traditional service areas and traditional measures of quality of service.

CONCLUSION

California supports migration of federal high-cost support to the CAF, and looks forward to working with the FCC to transition to an all IP-enabled communications world. However, due to concerns about how replacement of the current USF mechanisms for high cost support would impact customers served by California’s carriers and particularly customers of California’s rate of return carriers, the CPUC recommends that the FCC adopt a “glide path” that is reviewed in stages to measure the actual migration of traffic to IP, the impacts on end users, and the effects on ROR carriers. The CPUC further recommends that states remain responsible for implementing intrastate access charges in the revised environment, working cooperatively with the FCC on its “glide path” to eliminate access charges, reciprocal compensation and disparate rates for carrier and traffic types. We recommend that the FCC provide positive incentives to states to act on reducing intrastate access rates, such as preference for receipt of the first phase of the CAF funds. The CPUC also recommends there be a “no barriers” approach to measuring costs and revenues by supported carriers, in that regulated and unregulated

⁵¹ NPRM, at para. 600 (emphasis added).

revenue are considered. Finally, the CPUC urges the FCC to provide additional clarification as to how the CAF would support broadband deployment in practice, as discussed above.

Respectfully submitted,

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April 18, 2011